United States Court of Appeals

for the Second Circuit

APPELLANT'S REPLY BRIEF

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76-7082

To be argued by:
JOSEPH W. BURNS

B

United States Court of Appeals
FOR THE SECOND CIRCUIT

Docket No. 76-7082

P/S

MUNTERS CORPORATION,
Plaintiff-Appellee,

v.

BURGESS INDUSTRIES INCORPORATED,
Defendant-Appellee,

and

BUFFALO FORGE COMPANY,
Defendant-Appellant.

APPEAL FROM AN ORDER OF THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF NEW YORK
GRANTING A PRELIMINARY INJUNCTION

REPLY BRIEF FOR DEFENDANT-APPELLANT BUFFALO FORGE COMPANY

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UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

MUNTERS CORPORATION, Plaintiff-Appellee,	:	
v.	:	Docket No. 76-7082
BURGESS INDUSTRIES INCORPORATED, Defendant-Appellee, and BUFFALO FORGE COMPANY, Defendant-Appellant.	:	

I

THE TRANSACTION IS A
TRUE PATENT LICENSE

Burgess argues that the Munters/Buffalo Forge agreement is a sale rather than a patent license agreement. (Burgess' Brief p. 14*) It is evident that this is at best a tortured construction of the nature of the agreement. Even the court below regarded the issue as turning on whether the field of use restriction is valid. (App. 99)

*Subsequent references to Appellee's Brief will be indicated "B, p. __," to Appellant's Brief, "BF p. __" and to the Appendix, "App. __".)

The hallmark of an exclusive patent license has been defined in "14 Business Organizations - Patents - Costner and Einhorn - Patent Licensing Transactions," §1.01[2] as follows:

> "The patent grant gives the owner the right to exclude others from the enjoyment of the patented subject matter. Accordingly, a license in total effect amounts to an understanding on the part of the patent owner not to assert his right to exclude others against the licensee, if and when the licensee practices the invention. Essentially, this is true whether the license is exclusive or nonexclusive. An exclusive license merely adds the further undertaking on the part of the licensor not to enter into a similar agreement with any other party, or to assert the right to use the patent on his own behalf."

It is undisputed that:

(1) The plaintiff Munters has the exclusive rights under the U.S. patents to make, use and sell Munters fill with all the rights of an assignee.

(2) Munters fill is a patented product.

(3) Munters has granted to Burgess and Buffalo Forge non-exclusive licenses to use Munters fill in evaporative coolers for all applications other than with gas turbines of over 500 Horsepower.

(4) That Munters is the sole manufacturer of Munters fill, and has sold it to Burgess and Buffalo Forge.

The fact that the agreement also provides for the sale of the fill to Buffalo Forge does not change the legal nature of the agreement. Nor does it diminish the rights of either party granted by the patent laws with respect to the patented product.

The agreement grants to Buffalo Forge the exclusive right to use and sell Munters fill in evaporative coolers for gas turbine applications. In the negotiations between Munters and Buffalo Forge it was agreed that Buffalo Forge was qualified to become a purchaser of the fill and to use it in new evaporative coolers which Buffalo Forge was to design. Munters advised Buffalo Forge it would have a license to use the fill, and the negotiations related to which field of use would be exclusive and which non-exclusive. (App. 88-90)

There were two major monetary considerations received by Munters in return for the limited exclusive grant. There were no evaporative coolers of any type manufactured in the United States using Munters fill. There were no evaporative coolers using Munters fill for gas turbine applications anywhere in the world. First, Buffalo Forge offered to invest a considerable amount of money in the redesign of its units to enable it to incorporate Munters fill. Second, it also offered to spend considerable effort and money through its sales force to persuade potential customers of the advantages of the proposed new evaporative cooler. (App. 75-78, 88-90)

The value of the first consideration received by Munters was approximately $128,000 - the amount expended by Buffalo Forge to design a new evaporative cooler using Munters fill, and trying to develop the market for it. (App. 77-78, 89-89A)

Munters was assured of a minimum consideration under

the second item by requiring Buffalo Forge to purchase a minimum quantity of fill during each term of the license in order to maintain the exclusivity. This guaranteed profit was in lieu of a royalty, and was appropriate here since Buffalo Forge had to create the market. Article 2, paragraph 5 of the agreement provides: "No royalty shall be payable by Buffalo to Munters Florida under the sublicensed Fill Patents, the parties having provided for minimum purchase and payments in Article V hereafter." (App. 15, 16)

Article V provided that if Buffalo Forge did not purchase a minimum quantity during the first term ending December 31, 1973, it was required to pay Munters a specific sum for each cubic foot less than the minimum purchased. For the second term ending December 31, 1975, the minimum requirement was tripled, and for each of the next three terms quintupled. (App. 17-18*)

Article V further provided Munters with a guarantee against loss in the event that Buffalo Forge cancelled any orders after acceptance by Munters. It provided that Buffalo Forge would have to pay cancellation charges equal to (a) the direct cost of labor and materials actually expended towards the manufacture of the goods, (b) Munters overhead percentage on (a), and (c) a pro-rata share of the profits Munters would have realized on the completed order. These payments did not release Buffalo Forge from paying the specific penalty for failure to

*At the trial the complete text of the agreement was made available to Burgess' counsel and it was agreed that the terms that do not appear in the Exhibit would be kept confidential.

meet minimum requirements. (App. 19)

Article VI, paragraph 3 provided that if Buffalo Forge terminated the agreement on December 31, 1972 it had to pay a penalty. (App. 20)

Article VI, paragraphs 4 and 5 provide that notwithstanding the right of Buffalo to extend each term, Munters may cancel the exclusive grant if Buffalo does not purchase a minimum quantity, which increases with each term. (App. 20-23)

These provisions distinguish this license from a sale and prove that valuable and specific consideration was paid by Buffalo Forge, which was not paid by Burgess or other non-exclusive licensees.

II

THE BURGESS DISTINCTION OF GENERAL TALKING PICTURES IS CLEARLY ERRONEOUS

Burgess seeks to distinguish General Talking Pictures on the basis that it was only applicable to a manufacturing licensee, not a licensee who purchases and uses the patented product as a component in some other product. (B p. 10)

But the question addressed by the Supreme Court in its first opinion was "Can the owner of a patent by means thereof, restrict the use made of a device manufactured under the patent, after the device has passed into the hands of a purchaser in the ordinary channels of trade, and full consideration paid therefor." (304 U.S. at 177)

Burgess is in exactly the same position as GTP. Burgess purchased Fill from the manufacturer-licensee Munters. GTP purchased from the manufacturer-licensee The Transformer Company. Munters is not the patent owner - it is a licensee of A.B. Carl Munters which owns the patents. Transformer was a licensee of patent owner A.T. & T. Both Burgess and GTP had knowledge of the license restriction. Both contended that the license could not be used to restrict their use of the product, since the sale exhausted the patent monopoly. Under the Supreme Court's clear and specific ruling neither Burgess nor GTP was "a purchaser in the ordinary channels of trade."

The Supreme Court's conclusion in its first opinion does not turn on the issue of whether or not the licensee had the right to manufacture. It states:

> "Patent owners may grant licenses extending to all uses or limited to use in a defined field. *** Unquestionably, the owner of a patent may grant licenses to manufacture, use or sell upon conditions not inconsistent with the scope of the monopoly.*** There is here no attempt on the part of the patent owner to extend the scope of the monopoly beyond that contemplated by the patent statute*** There is no warrant for treating the sales of amplifiers to petitioner as if made under the patents or the authority of their owner." (304 U.S. at 181)

Furthermore, the subsequent opinion by the Supreme Court adds:

> "That a restrictive license is legal seems clear.*** As was said in United States v. General Electric Co., 272 U.S. 476, 489, the patentee may grant a license 'upon any condition the performance of which is reasonably within the reward which the patentee by the grant of the patent is entitled to secure.' The restriction here imposed is of that character. The practice of granting licenses for a restricted use is an old one***." (305 U.S. at 127)

United States v. Ciba Geigy Corporation (B-13), far from supporting Burgess, is a direct authority in support of Buffalo Forge. It is difficult to understand why Burgess would request this Court to accept a strained and irrelevant discussion of one part of that opinion, and expect the Court to blind itself to the remainder of the opinion. There were two entirely independent groups of agreements: (1) supply agreements, and (2) license agreements. The quotation on page 14 refers to the supply agreements, and not to the licenses. Burgess contends that the Munters agreement has the effect of restricting the use to which Burgess could put the patented fill. The Court held that was legal in Ciba Geigy.

The Ciba license to Abbott was in three parts. It provided for a sale of bulk HCT, and limited Abbott to the sale of HCT in specialty form. It also granted Abbott the right to make, use, and sell HCT in specialty form. The government contended that the license agreement amounted to a per se violation of Section 1 of the Sherman Act, or alternatively, under the rule of reason or the doctrine of ancillary restraints, the license violated Section 1.

The Court held the agreement valid, cited General Talking Pictures and said:

> "To say that CIBA 'restrained competition' by not licensing Abbott in as unlimited a fashion as possible is to impose a duty upon the patentee that simply is not justifiable. The restraint on competition inheres in the patent monopoly itself." (p. 64)

And further:

"Any limitation contained in a patent license, by definition, results in a restraint in trade. The restraint inheres in the grant of the patent itself which by its terms conveys the power to exclude. Therefore, it seems fruitless to attempt to judge the legality of a particular limitation contained in a license in terms of the competition it prevents from coming into existence." (p. 60)

Burgess is complaining because Munters has declined to give it an unlimited license to use Munters fill. All that is necessary is to change the names in the above citation so it reads:

"To say that Munters 'restrained competition' by not licensing Burgess in as unlimited a fashion as possible is to impose a duty upon the patentee that simply is not justified."

III

THE LICENSE AGREEMENT DOES NOT UNLAWFULLY RESTRICT THE USE OF MUNTERS FILL BY BURGESS' CUSTOMERS

Burgess also relies upon the language of Article II, paragraph 1 of the Agreement (App. 14) to support its contention that the paragraph restricts its customers from using Munters fill inside the exclusive area. Burgess argues that its customers are restricted in the use which they may make of Munters fill following a purchase from Munters by Burgess. (B 15-18) It is important to note that neither Buffalo Forge nor Burgess "resell" the Munters fill. They incorporate the fill in an evaporative cooler, and it becomes an integral part of the cooler, like a piece of metal or a valve. The restriction is solely against Burgess.

Both Burgess and Buffalo Forge have non-exclusive rights to use Munters fill in any application except with gas turbines. Buffalo Forge has the further exclusive right to use Munters fill with gas turbines.

All fill sold by Munters to Burgess may be used by Burgess' customers in any evaporative coolers in which Munters has licensed Burgess to use the fill. To avoid confusion, the Court should note that an evaporative cooler designed for use with a gas turbine cannot physically be used in any other application. Evaporative coolers for industrial use are of a different design. Munters has not sold any fill to Burgess for use in a gas turbine application. When Burgess did use the fill in the restricted product use area, it was an infringer under the General Talking Pictures decision. There was only one instance where Burgess sold to a customer (Westinghouse) an evaporative cooler for use with a gas turbine. In that instance Burgess gave Westinghouse a "hold harmless" letter, since Westinghouse was aware of the restriction on Burgess. (App. 68) Whether or not Westinghouse could use the cooler without infringing is not an issue in this case, and should not be considered by this Court.

Since this language in Article II, paragraph 1 of the agreement is in accord with General Talking Pictures, it can hardly be considered to create a serious issue for purposes of preliminary injunctive relief.

IV

WITH RESPECT TO SECURITY, BUFFALO FORGE SEEKS NO PRESENT INCREASE IN THE AMOUNT OF THE BOND

Burgess misconceives the thrust of the procedural relief sought by Buffalo Forge. No present increase in the amount of the security was sought. The sole relief requested was an order requiring Burgess (1) to notify it of all contracts that it may receive which employ Munters fill in the area of exclusivity and (2) to provide the attorneys of Buffalo Forge with the opportunity to review under appropriate safeguards of confidentiality all internal documents of Burgess relating to its profit calculations for each such contract.

Through the use of such procedure, Buffalo Forge might periodically move the Court below to increase the amount of security to reflect the amount of profit lost to Buffalo Forge until a final decision on the merits of this case. (See BF 62-63, App. 110)

V

CONCLUSION

Insofar as appellant's research of the law has disclosed this is the first preliminary injunction that has completely vitiated a patent license agreement during the

pendency of litigation concerning that patent license. The record below fails to support it and the Court below made material errors in construing the law. The injunction should be vacated.

Respectfully submitted,

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